INDIANA DEPARTMENT OF REVENUE

REVENUE RULING #2001-08IT

August 1, 2001

Notice: Under IC 4-22-7-7, this document is required to be published in the Indiana Register and is effective on its date of publication It shall remain in effect until the date it is superseded or deleted by publication of a new document in the Indiana Register. The publication of this document will provide the general public with information about the Department's official position concerning a specific issue.

ISSUES

Treatment of single member LLC electing under federal check-the-box regulations to be treated as a disregarded entity.
Authority: Tax Policy Directive # 2

Qualification of company a taxpayer under Indiana Financial Institutions Tax ("FIT").
Authority: IC 6-5.5 et seq.

Treatment of income earned by a Factoring company under Indiana FIT.
Authority: IC 6-5.5 et seq.

Attribution of interest income under Indiana FIT.
Authority: IC 6-5.5-4-5

Elimination from Indiana gross income tax ("GIT") of income and deductions by member of a unitary group subject to GIT and another member of the unitary group subject to FIT.
Authority: IC 6-2.1-2-11

Elimination of sales between members of unitary group, in computation of apportionment factor.
Authority: 45 IAC 3.1-1.51 and 45 IAC 3.1-1-52

Classification and attribution of interest income derived from inter-company loans under FIT
Authority: IC 6-5.5-4-6

STATEMENT OF FACTS

Co. A is a publicly-traded Delaware corporation commercially domiciled in Indiana and taxed under subchapter C of the Internal Revenue Code of 1986 (IRC). Co. A is primarily a holding

company with a number of operating subsidiaries. The largest operating subsidiaries are Co. B and Co. C.

Co. B is a Delaware limited partnership that has elected to be taxed as a corporation for federal and state income tax purposes. Co. B is commercially domiciled in Indiana and manufactures its products at facilities in Iowa, Tennessee, and Indiana. Co B sells its products to Co. C and to unrelated third parties throughout the United States. The partners of Co. B are Co. A, which is a 99% limited partner, and Co. C, which is a 1% general partner.

Co. C is a wholly owned subsidiary of Co. A, incorporated in Delaware and headquartered in Missouri. Co. C operates retail locations throughout the United States. These retail locations sell new and used products and parts for products. These locations also perform repair and maintenance services.

Co. A and its subsidiaries file a consolidated return for federal income tax purposes, and Co. A files an Indiana consolidated adjusted gross income tax return that includes those subsidiaries that have income from Indiana sources, including Co. B and Co. C. On a consolidated basis, the affiliated group generates in excess of $1 billion of revenue.

Co. B and Co. C make credit sales to customers and, therefore, generate accounts receivable in the normal course of their business operations. Some of these credit sales are made to Indiana customers. Co. B and Co. C offer a variety of payment terms to their customers. Some customers pay by check sent to lockbox locations and others pay by electronic funds transfer.

In order to achieve the most favorable borrowing rates against which the accounts receivable could be used as collateral, Co. B and Co. C plan to participate in an asset-backed securitization program with a national banking corporation and its conduit.

Co. A is considering creating a new corporation, Co. D, as a wholly owned subsidiary of Co. A. Co. D will be a corporation taxed under subchapter C of the IRC and commercially domiciled in Indiana. [Note: Co. D may be formed as a single member LLC electing to be taxed as a corporation] Co. D will have employees who will perform credit and collection services, cash applications, and oversight of the factoring and securitization program. Co. D cannot participate in asset-backed securitization programs because its operations do not enable it to qualify as a "bankruptcy remote" entity. Therefore, Co. D will create a single member limited liability company (Co. E). Co. E will qualify as a special purpose "bankruptcy remote" entity, as its activities will be limited to acquiring, owning, and financing accounts receivable. Co. E is prohibited from having other types of operations in order to qualify as a "bankruptcy remote" entity. Co. E will be a disregarded entity for federal income tax purposes and treated as a division of Co. D.

Co. D will purchase accounts receivable for cash without recourse, at an arm's length discount, from Co. B and Co. C. Co. D will sell to Co. E all or a portion of the accounts receivable purchased from Co. B and Co. C for cash, without recourse, at a discount. This transaction will be characterized as a sale for commercial law purposes. For federal income tax purposes, this

transaction and all other transactions between Co. D and Co. E will be treated as intracompany transactions because Co. E is treated as a division of Co. D.

Co. E will sell the accounts receivable purchased from Co. D to a national banking corporation and its conduit. For federal income tax purposes, Co. E will be treated as having borrowed funds from the national banking corporation and its conduit. Since Co. E will be treated as a division of Co. D for federal income tax purposes, all transactions entered into by Co. E will be treated as entered into by Co. D.

In addition to the income that it will earn as a result of the recovery of portions of the discount on the accounts receivable that it will purchase from Co. B and Co. C, Co. D will also earn interest on short-term investments of cash collections pending purchase of new accounts receivable and interest on intercompany loans that it makes to its affiliates, including Co. B and Co. C for general working capital.

RULING

Based solely and strictly on the information submitted in the request for ruling dated July 11, 2001, a copy of which is incorporated herein by reference, the Department hereby rules as follows:

1. Co. E will be classified as a disregarded entity under the federal "check-the-box" regulations and will be treated as a division of Co. D. (Note: Co. D may be formed as a single member LLC electing to be treated as a corporation for federal tax purposes.) For tax purposes Indiana will also treat Co. E as a division of Co. D in accordance with the provisions of Tax Policy Directive #2.

2. Under the analysis of its proposed business activity, Co. D will qualify as a taxpayer under the Indiana Financial Institutions Tax ("FIT") and shall report and pay any tax, which may be due, under the provisions of IC 6-5.5 et seq.

3. Co. D's income from the collection of accounts receivable will be the difference between the amount paid by customers in satisfaction of their accounts receivable and the amount paid by Co. D to purchase the accounts receivable from Co. B and Co. C. Since this discount will be derived from the prevailing market rates of interest and the creditworthiness of Co. B's and Co. C's customers, the recovery of this discount by Co. D will be classified as interest income under IC 6-5.5.

4. Co. B and Co. C sell products to their customers on credit. Under the proposed transactions, it would appear this extension of credit by Co. B and Co. C to their customers would constitute a consumer loan. Co. D will purchase these customer accounts receivable from Co. B and Co. C without recourse. The customers of Co. B and Co. C as obligors on the accounts receivable, will become customers of Co. D at the time the accounts receivable are sold. Co. D's interest income will be attributable to Indiana under IC 6-5.5-4-5 if such loans are made to an Indiana resident. Indiana will deem any

customer to be an Indiana resident if such customer is commercially domiciled within Indiana or if such customer maintains a business situs within Indiana and such business situs is directly engaged in the sales transaction with Co. B or Co. C regardless of the company location from which the payment on the account receivable may be remitted.

5. Co. D will be included in the federal consolidated income tax return currently filed by the parent and its subsidiaries. For Indiana gross income tax ("GIT"), if an entity is subject to GIT and is a member of a unitary group of which a taxpayer subject to FIT is also a member, all income and deductions attributable to transactions between the entity and the unitary taxpayer which is subject to the FIT shall be eliminated in determining the amount of GIT imposed under IC 6-2.1-2-11. Thus Co. B and Co. C's receipts from the sale of accounts receivable to Co. D will not be subject to GIT. Additionally, any dividends that Co. A may receive from Co. D will not be subject to GIT.

6. Under the proposed transactions, Co. B and Co. C will have receipts from the sale of accounts receivable to Co. D, despite the fact that the accounts receivable will be sold at a discount, and Co. B and Co. C will have no net gain on these transactions. 45 IAC 3.1-1-51 provides that the denominator of the sales factor shall not include sales made between members of an affiliated group filing consolidated returns. 45 IAC 3.1-1-52 provides that the numerator of the sales factor shall not include sales made between members of an affiliated group filing consolidated returns. It is not the Department's position to penalize members of an affiliated group who would otherwise qualify to file a consolidated Indiana income tax return simply due to the requirement that a member would be required to file under IC 6-5.5. The Department therefore rules that Co. B and Co. C's receipts from the sale of accounts receivable to Co. D will be eliminated for purposes of the computation of Co. B and Co. C's apportionment factors for Indiana adjusted gross income tax and Indiana supplemental net income tax calculations.

7. For purposes of the Indiana FIT, Co. D's interest income from intercompany loans that it may make to affiliates for general working capital purposes shall be treated as interest income from unsecured commercial loans and attributed in accordance with IC 6-5.5-4-6. IC 6-5.5-4-6 provides that interest income from unsecured commercial loans must be attributed to Indiana if the proceeds of the loan are to be applied in Indiana. If it cannot be determined where the funds are to be applied, the income and receipts are attributed to the state in which the business applied for the loan. "Applied for" shall mean the initial inquiry or submission of a completed loan application, whichever occurs first.

CAVEAT

This ruling is issued to the taxpayer requesting it on the assumption that the taxpayer's facts and circumstances, as stated herein, are correct. If the facts and circumstances given are not correct, or if they change, then the taxpayer requesting this ruling may not rely on it. However, other taxpayers with substantially identical factual situations may rely on this ruling for informational purposes in preparing returns and making tax decisions. If a taxpayer relies on this ruling and the Department discovers, upon examination, that the fact situation of the taxpayer is different in

any material respect from the facts and circumstances given in this ruling, then the ruling will not afford the taxpayer any protection. It should be noted that subsequent to the publication of this ruling, changes in statute, a regulation, or case law could void the ruling. If this occurs, the ruling will not afford the taxpayer any protection.

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